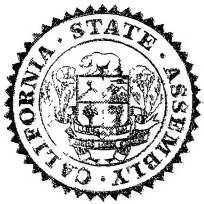


REPORT OF THE
OFFICE OF THE AUDITOR GENERAL
TO THE
JOINT LEGISLATIVE AUDIT COMMITTEE

715.3

THE FOUNDATIONS' EXPENDITURES
NEED REVIEW AND CONTROL

DECEMBER 1977



Joint Legislative Audit Committee

OFFICE OF THE AUDITOR GENERAL

California Legislature



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December 27, 1977

The Honorable Speaker of the Assembly
The Honorable President pro Tempore of the Senate
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members of the Legislature:

Your Joint Legislative Audit Committee respectfully submits the Auditor General's report on the use of funds raised by nonprofit corporations (foundations) for the benefit of the University of California. University President David S. Saxon acknowledges the need for improved controls either by the University where appropriate or by pointed suggestion to the trustees of the several foundations. The analysis by the University staff, on the other hand, has all the class of a sea lawyer.

By copy of this letter, the Department is requested to advise the Joint Legislative Audit Committee within sixty days of the status of implementation of the recommendations of the Auditor General that are within the statutory authority of the Department.

The auditors are Kurt R. Sjoberg, Audit Manager; Ross A. Luna; and Daniel G. Perez.

Respectfully submitted,

MIKE CULLEN
Chairman

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SUMMARY

The University of California (U.C.) has nine campus-affiliated foundations which are organized to solicit gifts, endowments and other financial assistance from private sources on behalf of the U.C. Regents. Although all of the campus foundations are separately organized under the General Non-Profit Corporation Law of California, they are closely associated with the U.C., have offices on campus and use certain university property and equipment rent-free.

We reviewed the operations of the four campus foundations at U.C. Davis, Los Angeles, Santa Barbara and Santa Cruz for fiscal years 1975-76 and 1976-77. We tested expenditures from major accounts and determined to what extent they were made in accordance with university regulations and foundation policies.

We found that:

- Foundations have made certain expenditures which would not have been allowed if they were made from university-controlled or state funds. These expenditures, which totaled about \$90,000 for the period, included first-class travel, entertainment and membership fees in social organizations for university staff and guests (see page 7).

Three of the foundations, however, have recently established policies which should control some of the expenditures of this type (see page 9).

- Foundations have inadequately controlled the disbursement of funds and have failed to disclose certain expenditures to the Internal Revenue Service. These expenditures resulted primarily from a lack of internal control by appropriate foundation and university officials (see page 13). The foundations have effected new controls and are recovering some of these payments (see page 14).

We recommend that the University adopt a consistent systemwide policy to assure that all campus foundations expend funds in conformity with U.C. policies and establish controls over the funds as necessary. We also recommend that the U.C.'s Internal Audit and the foundations' legal counsels, respectively, make follow-up audits and consider the legal aspects of the foundations' failure to report to IRS (see pages 12, 17 and 18).

INTRODUCTION

In response to a resolution of the Joint Legislative Audit Committee, we are reviewing a number of the operations of the University of California (U.C.). This is our third in a series of reports on the U.C.* This report addresses the U.C. campus foundations' programs and operation.

The U.C. has nine campus-affiliated foundations which are organized under the provisions of the General Non-Profit Corporation Law of California. All foundations are exempt from federal income and California franchise taxes but are required to file periodic information returns on their operations. The foundations' primary purposes are to solicit gifts, endowments and other financial assistance for the U.C. Regents.

Five of the foundations (Berkeley, Davis, Los Angeles, Irvine and San Diego) are considered major campus foundations. The first three were originated as auxiliaries of pre-existing university alumni associations as a means of consolidating and intensifying gift solicitation efforts. The other two were not initially alumni-based foundations and are relatively new. All five major foundations, however, have virtually the same organizational structure and purposes for operating.

* Earlier reports are U.C. Davis Child-Rearing Practices and Academic Abilities Research Project (Letter Report 715.1), August 1977, and The Patent and Royalty Program of the University of California (Report 715.2), October 1977.

The four other U.C. foundations (Riverside, Santa Barbara, Santa Cruz and San Francisco) are smaller foundations. Their organizational structures and purposes, however, are similar to those of the U.C.'s major campus foundations.

The foundations' business affairs are conducted by their respective Boards of Trustees or Directors. In general, the trustees or directors serve on the board without extra compensation. However, some foundation boards are empowered to determine the compensation to be paid to the foundation's personnel including the trustees and directors.

Two or more trustees, directors or officers of each foundation we visited during the audit were also officers or staff employees of the U.C. campus administration.

The campus foundations use university-salaried personnel and university working facilities to carry out their financial affairs and administrative functions. This practice also appears to be common among other nationally known educational institutions. The advantages of this arrangement are economic considerations and closer working relationships between the universities and their respective foundations.

The principal offices of the U.C. foundations are located on the university campuses. Certain property including furniture and equipment belonging to the U.C. Regents is used rent-free by the campus foundations. Also, certain activities of some of the U.C. foundations are integrated with those of the alumni associations and the university fund-raising activities. The expenditures for salaries and other reimbursable expenses are classified as the foundations' shares of such expenditures based on budget allocations or funding arrangements among the three entities.

Scope of Review

Of the nine U.C. campus-affiliated foundations, four (two major and two small) foundations were selected for review. We tested and verified material receipts (over \$10,000) from donors by referring to records and documents evidencing transmittal and deposit of the funds for fiscal years 1975-76 and 1976-77. The foundations' restricted funds and general fund accounts having annual expenditures of \$1,000 or more per account were vouched to check payments and underlying invoices, receipts and other supporting documentation. The propriety of the expenditures was measured against existing university guidelines governing expenditure payments or reimbursements to determine whether the expenditures incurred by the foundations would have been allowable under university rules and regulations. We also compared expenditures to foundation articles of incorporation to assure compliance. The results of the vouching procedure are discussed in more detail in the succeeding section of this report.

We reviewed the organizational structures of the U.C. foundations and their relationships with the university campus administration and/or alumni associations. We also compared the foundations' organizations and activities with those of other states' university foundations. The responses from this survey of selected universities indicated that most foundations, although separate and independent entities, work closely with the universities and play an important role in the development and fund-raising programs of these universities.

Available audited or unaudited financial statements of the four U.C. campus foundations for the two applicable fiscal years were reviewed and analyzed. We did not perform a complete financial audit of the U.C. foundations; therefore, we do not express an opinion on the foundations' fiscal year 1975-76 and 1976-77 financial statements.

At the request of UCLA Foundation officials and to avoid duplication of audit work already done by the foundation's external auditors, we reviewed the auditors' working papers covering their examination of the 1975-76 foundation accounts. Oral representations made by the foundation's officers and staff were verified and referenced to support data and schedules available to us during our review of the audit working papers.

AUDIT RESULTS

CERTAIN DISBURSEMENTS MADE BY CAMPUS-
AFFILIATED FOUNDATIONS WOULD NOT HAVE
BEEN ALLOWED BY THE UNIVERSITY

Our review of four U.C. campus-affiliated foundations for fiscal years 1975-76 and 1976-77 disclosed that the foundations made certain expenditures of private funds solicited on behalf of the University which, if incurred by the University under its policies and rules governing expenditures, would normally be disallowed for payment or reimbursement out of university-controlled or state funds. These expenditures, which totaled about \$90,000 for the two years reviewed, included first-class travel, entertainment and membership fees in social organizations primarily for university staff and guests. Although the foundations are not presently required by the University to follow U.C. regulations, they are so closely aligned that independence from the U.C. is not clearly established. At issue is whether the University wishes the foundations to continue to operate on their behalf while making some expenditures which would not be allowed by the U.C. itself.

In July 1976, the U.C. President announced that any gift solicited on behalf of the U.C. Regents would be administered in compliance with university policies. He delegated the responsibility of enforcing this regulation to the chancellors of the various campuses.

We found no university-written guidelines categorizing the types of allowable and unallowable expenditures.* The absence of such guidelines afforded the foundations an opportunity to pay or reimburse expenditures which were not compatible with U.C. policies and practices.

Examples of the expenditures are tabulated in Appendix C (Items 1-5). Most of the expenditures were incurred by the two major foundations we visited: The UCLA Foundation, Los Angeles campus; and California Aggie Alumni Foundation, Davis campus. These expenditures benefited university employees as well as foundation staff and guests. Some of the purchases were: liquor and other alcoholic beverage purchases, \$7,923; membership fees in organizations which are primarily social, \$22,985; and first-class air fares, \$3,296.

Are Foundations Independent?

Although the chancellors have been delegated the authority by the U.C. President to require that organizations soliciting gifts comply with university policies, the articles of incorporation of the individual campus foundations indicate that the foundations are legal entities separate from the University. There is an unavoidable relationship between the two, however, since the foundations' main purpose is to aid and provide financial assistance through gifts, endowments and other means to the university campus. In addition,

* See page 9 for recent guidelines.

many foundations are provided the use of university property rent-free (Appendix A), and the U.C. Regents are the sole and ultimate beneficiary in case of dissolution and asset liquidation of some of the campus foundations.

The purposes for which the campus foundations were formed, the nature of their fund-raising activities and the close working relationships prevailing between the foundations and the University are, we believe, ample proof that the foundations are not, in effect, entities totally separate and independent from the University.

New Policies Affecting Some Foundations

Three of the U.C. campuses we visited have recently established policies which impact upon their foundations. In September 1977, the Davis administration limited university staff and faculty from authorizing, directing or recommending the expenditure of funds donated for university purposes until the funds are tendered to the U.C. Regents. Also in September, the UCLA Chancellor directed the UCLA Foundation to discontinue the direct disbursement of funds and make all expenditures through UCLA in accordance with university regulations. In addition, in June 1977 the U.C. Santa Cruz established control over the expenditure of funds from gifts received for a specific university program.

The policies detailed below have varying impact on the foundations:

U.C. Davis

Effective in September 1977, the Chancellor's Office established that university staff and faculty shall not authorize, direct or recommend the expenditure of funds from gifts donated for university purposes or in support of university programs, which funds are held by an individual or organization other than the University, unless and until such funds have been transferred to the University through a tender of gifts to the U.C. Regents. The expenditure of such funds shall thereafter be subject to the terms of the gift and established university policy.

U.C. Los Angeles

The UCLA Foundation previously disbursed funds in one or both of two methods: (1) by means of a gift to the University whereby funds are made available for expenditure by the University through normal university channels and (2) by direct disbursements by the Foundation without university involvement. Effective in September 1977, the UCLA Chancellor directed the Foundation to discontinue direct disbursements. The discontinuance affected the disbursements of funds only and did not change the policies relating to the establishment or investment of restricted foundation funds.

U.C. Santa Cruz

Effective in June 1977, the University established that gifts received by the Foundation for the benefit of a specific university program or departmental unit shall be awarded to the U.C. Regents in the month of receipt, and corresponding cash shall be transmitted to the University on or by the last working day of the same month. The expenditures from the gifts shall be incurred and recorded by the University under its established policy.

CONCLUSIONS

The lack of university-wide policies regarding the relationship of the various campuses and their foundations has resulted in either nonexistent or inconsistent control over the expenditures made by the foundations. Consequently, expenditures have been made on behalf of the University which do not comply with university regulations.

Although the UCLA, U.C. Davis and U.C. Santa Cruz campuses have recently established policies regarding their foundations, they are inconsistent and have varying impact.

RECOMMENDATIONS

We recommend that the U.C. Systemwide Administration:

- Adopt a consistent systemwide policy designed to effectively control and monitor the foundations' expenditure of funds in conformity with accepted university policies
- Instruct its internal audit staff to make independent periodic reviews of the foundations to ensure that the U.C.-prescribed policies and procedures are being observed.

BENEFITS

Properly implementing the above recommendations would assure both university and foundation management of better and more effective control over the use of foundation funds.

THE FOUNDATIONS HAVE INADEQUATELY CONTROLLED
AND DISCLOSED CERTAIN EXPENDITURES

Our review of the foundations' records, procedures and controls disclosed:

- Weaknesses in internal accounting control over the foundations' system for expenditure disbursements, and several questionable expenditures by the two major U.C. campus foundations which totaled more than \$85,000
- Unreported transactions by the U.C. campus foundations which were omitted in preparing and filing federal information returns to the Internal Revenue Service (Form 990).

Inadequate Controls

The internal control weaknesses in the disbursement of funds resulted primarily from the lack of proper review and control by appropriate foundation and/or university officials before the payments were made. Examples of the foundations' expenditures made on behalf of university staff and guests, which are shown as Items 6-10 in Appendix C, included travel advances for which no accounting was rendered by university employees, \$12,632; double payments for air travel expenses, \$1,652; direct reimbursements or payments with inadequate or no supporting documents, \$37,955; and payments to staff and others which were considered unusual and personal in nature,

such as professional society dues, car lease payments, purchases of athletic event tickets, etc., \$23,661. Also, the two major U.C. foundations contributed \$11,975 for political purposes during the fiscal years under review contrary to the foundations' articles of incorporation and by-laws.

The UCLA Foundation trustees, acting on recommendations of the foundations' external auditors, have put into effect new controls on staff spending. This resulted from the auditor's discovery of questionable expenditures of foundation funds. Since this discovery, the Foundation has recovered substantial losses through cash restitution and by a secured promissory note.

The double travel payments involved university employees whose air fares were reimbursed to them by both the California Aggie Alumni Foundation and U.C. Davis campus. We were advised that the situation is now being rectified and that the employees concerned have been instructed to refund to the Foundation the amounts paid for air travel.

Inadequate Disclosures

Tax-exempt foundations are required by the Internal Revenue Service (IRS) to file annual information returns on Form 990. To determine current exemption status, the foundations are also required to report any changes in the organization's purposes and character or method of operation.

Our review of the 1975-76 information returns prepared by the four U.C. campus foundations we visited showed that the UCLA Foundation, Los Angeles; California Aggie Alumni Foundation, Davis; and the UCSB Foundation, Santa Barbara; omitted disclosures of certain pertinent information on Form 990, contrary to instructions on the form.

We are unaware of the total potential impact that nondisclosures of the information will have on the foundations. However, omitting essential facts and figures called for in the applicable sections of Form 990 might result in assessable penalties (unless reasonable cause is shown) with respect to failure by the foundations to file correct information returns.

The omitted information in the 1975-76 returns consisted of:

<u>Nature of Transactions</u>	<u>Foundation</u>
(1) Amounts expended directly or indirectly for political purposes	UCLA Cal Aggie
(2) Purchases of securities (through foundation trustee) from a stock brokerage firm with which such trustee is affiliated	UCSB
(3) Furnishing of goods or services by organizations involving the foundation and the personal or business affairs of member trustees who are affiliated with such organizations	UCLA
(4) Additional compensation payments to foundation officers or employees whose salaries were being paid through the university payroll system	UCLA

The above-listed transactions were also contrary to the foundations' articles of incorporation and by-laws which provide that:

- The foundation shall not carry on propaganda or otherwise attempt to influence legislation and shall not participate in, or intervene in any political campaign on behalf of any candidate for public office.
- The foundation does not contemplate pecuniary gain or profit to the members thereof, and it shall at all times be operated in such manner as to entitle it to exemption under Section 501(c)(3) of the Internal Revenue Code.

Because of the propriety and impact of the transaction as they affect the status of the tax-exempt foundations organized under IRS rules, we believe that the foundations' legal counsels should be consulted to determine whether, under the present circumstances, amended information returns should be filed with the tax authorities to include the unreported transactions.

By the end of our fieldwork, none of the four* U.C. campus foundations had filed their respective information returns for the fiscal year ended June 30, 1977. Since similar transactions described

* Three foundations have since filed their 1976-77 returns on the dates indicated as follows: Cal Aggie Alumni Foundation--11/15/77; U.C. Santa Cruz Foundation--11/7/77; UCSB Foundation--11/15/77.

and listed on page 15 of this report were also made in fiscal year 1976-77 by the UCLA Foundation, California Aggie Alumni Foundation and UCSB Foundation, such transactions should be reported by these foundations when filing their 1976-77 information returns in order to fulfill the IRS requirements.

CONCLUSIONS

The lack of proper review and control by appropriate foundations' officials has resulted in ineffective control and monitoring over the expenditure of funds. The campus foundations at U.C. Los Angeles and Davis have begun to rectify the situation, however.

In addition, the U.C. campus foundations at Los Angeles, Davis and Santa Barbara appear to be in violation of IRS requirements for reporting information on Form 990. The foundations' failure to comply with the requirements may result in assessable penalties for filing incorrect information returns.

RECOMMENDATIONS

We recommend that the U.C. administration and foundation officials confer and review the propriety of expenditures and the adequacy of documentation in support of payments made on behalf of the University and develop controls as necessary.

We also recommend that the U.C. administration and the affiliated foundations develop effective controls and procedures to preclude the recurrence of double expenditure reimbursements under the present dual disbursement system of the U.C. and foundation accounting offices.

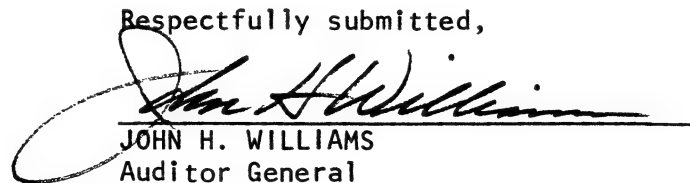
We further recommend that the UCLA Foundation, California Aggie Alumni Foundation and the UCSB Foundation:

- Consult with legal counsel to determine whether amended information returns should be filed with the IRS to include the unreported transactions
- Include such similar transactions made by the foundations in 1976-77 when preparing and filing Form 990 with the IRS for the fiscal year.

BENEFITS

Implementing these recommendations would assure adequate control over the expenditure of funds and proper reporting of the foundations' transactions and information required by the IRS. Moreover, any penalties for improper return filing would be avoided.

Respectfully submitted,



JOHN H. WILLIAMS
Auditor General

Date: December 22, 1977

Staff: Kurt R. Sjoberg, Audit Manager
Ross A. Luna
Daniel G. Perez

WRITTEN RESPONSE TO THE AUDITOR GENERAL'S REPORT

The following is the response to our report by U.C. President, Dr. David S. Saxon. We have footnoted areas which we felt needed discussion or clarification. The footnotes are summarized on page 31.

UNIVERSITY OF CALIFORNIA SYSTEMWIDE ADMINISTRATION

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Office of the President

BERKELEY, CALIFORNIA 94720

December 19, 1977

Mr. John H. Williams, Auditor General
Joint Legislative Audit Committee
925 "L" Street, Suite 750
Sacramento, California 95814

Dear Mr. Williams:

In response to your letter of December 13 I attach a staff analysis, in which I concur, of the audit findings and recommendations resulting from your review of the operations of campus foundations. I would like to add some comments.

Foundations make very useful contributions to the University and are an important and vital element in the voluntary support which the University enjoys. Many of their accomplishments flow from their flexibility as legally independent entities. As a result, they have the capacity to assist the University in many important areas.

The audit findings do reveal that action by the Foundations to improve certain of their administrative practices is in order. The University concurs in this.

We will assist the foundations in improving procedures and practices and installing adequate controls, and will offer our guidance in achieving these goals. This will be carried out in a manner consistent with the organizational independence of the foundations. In addition, the University is beginning to explore the formulation of a uniform policy which would govern its relations with the foundations.

We are pleased that your audit report acknowledges recent individual campus efforts to furnish guidance in foundation operations. It is noted, however, that a number of the audit findings and recommendations identify matters for which the foundations, as legal entities, must assume responsibility for corrective action. I will provide the chairpersons of the governing boards of the four foundations concerned with a copy of your report and this response and will encourage their efforts to take every appropriate action to respond to your findings and recommendations.

Mr. John H. Williams
December 19, 1977
Page Two

I regret that a more comprehensive response could not be prepared within the time available. We may wish to amplify our response at a later time.

Sincerely,



David S. Saxon
President

Attachment

cc: Chancellor James H. Meyer
Chancellor Robert Huttenback
Chancellor Robert Sinsheimer
Chancellor Charles E. Young
Special Assistant Lowell Paige

ANALYSIS OF DRAFT REPORT OF THE OFFICE
OF AUDITOR GENERAL ON FOUNDATION EXPENDITURES

Following is an analysis of the audit results and recommendations as set forth in the Auditor General's draft report on expenditures of foundations organized and located at campuses of the University of California to solicit gifts and other financial assistance in support of the University.

Audit Comment

In the first paragraph of the Summary on page 1 of the report the statement is made that the foundations "solicit gifts, endowments and other financial assistance... on behalf of the U.C. Regents (emphasis added)."

Response

This is an incorrect statement which appears consistently throughout the report and leads to improper conclusions concerning the applicability of University policies and procedures to and University control over foundations. "On behalf of" implies that The Regents have authorized the formation of the foundations and directed them to solicit funds for The Regents. However, foundations have been voluntarily organized, are legally independent of The Regents, and solicit gifts on their own behalf in support of University activities. (1/)

Audit Comment

On page 5, in discussing the review of foundation expenditures, the report states that the "propriety of the expenditures was measured against existing university guidelines governing expenditure payments or reimbursements to ensure that the expenditures incurred by the foundations were allowable under university rules and regulations." (2/)

Response

The foundations are legally independent entities. While obviously they should adhere to good business practices in the expenditure of funds under their control, there is no legal requirement that they observe university rules and regulations in the expenditure of such funds.

Audit Comment

The report, on page 7, states that in July 1976 a pronouncement of the President provided "that any gift solicited on behalf of the U.C. Regents would be administered in compliance with university policies."

Response

The specific statement of the President was that "gifts to The Regents shall be administered in compliance with University policies and practices." The audit report appears to place a connotation on the pronouncement which would make it applicable to gifts to foundations. However, a foundation solicits gifts in its own name and the pronouncement as actually stated would be effective only when a foundation, in turn, donates funds to the University. (3/)

Audit Comment

On page 8 the report states that "We found no university-written guidelines at the foundations we visited categorizing the types of allowable and unallowable expenditures. The absence of such guidelines afforded the foundations an opportunity to pay or reimburse expenditures which were not compatible with U.C. policies and practices."

Response

Since the foundations are legally independent it is not appropriate for the University to issue guidelines governing the allowability of expenditures made by the foundations. Furthermore, such expenditures need not be in accord with policies governing the University. (1/, 3/, 4/)

Audit Comments

On page 11-12 of the report the following conclusions are drawn and recommendations made:

The lack of university-wide policies regarding the relationship of the various campuses and their foundations has resulted in either nonexistent or inconsistent control over the expenditures made by the foundations. Consequently, expenditures have been made on behalf of the University which do not comply with university regulations.

Although the UCLA, U.C. Davis and U.C. Santa Cruz campuses have recently established policies regarding their foundations, they are inconsistent and have varying impact.

We recommend that the U.C. Systemwide Administration:

- Adopt a consistent systemwide policy designed to effectively control and monitor the foundations' expenditure of funds in conformity with accepted university policies
- Instruct its internal audit staff to make independent periodic review of the foundations to ensure that the U.C.-prescribed policies and procedures are being observed.

Response

While systemwide guidelines for the relationship of the campuses to their foundations may be appropriate, the control over and monitoring of expenditures is strictly a foundation matter. There is no requirement that foundations, as legal entities, must comply with university regulations or be subject to University control. However, the University can and will encourage the foundations to adopt appropriate policies governing the expenditure of funds.

In view of the legal status of foundations, it is not appropriate for the University's internal audit division to conduct reviews of the foundations. The foundations have annual audits conducted by independent public accounting firms.

(1/)

Audit Comments

On page 13 the following audit findings are reported:

Our review of the foundations' records, procedures and controls disclosed:

- Weaknesses in internal accounting control over the foundations' system for expenditure disbursements and several questionable expenditures by the two major U.C. campus foundations which totaled more than \$85,000.
- Unreported transactions by the U.C. campus foundations which were omitted in preparing and filing federal information returns to the Internal Revenue Service (Form 990).

Response

Weaknesses in internal control and the proper reporting of transactions on IRS forms are matters to which the foundations should give attention. A copy of this report will be provided to the chairpersons of the respective governing boards of the foundations so that appropriate action can be taken. However, the following information concerning expenditures which have been considered questionable should be conveyed to provide a more complete and accurate record of the transactions and the overall situation.

First with respect to the questioning of alcoholic beverage purchases, one must consider the circumstances surrounding such purchases before alleging improprieties. Even University entertainment policy permits such purchases provided State General Funds and certain other funds are not used (see Exhibit I).

With respect to social club memberships, one must again look at the circumstances relating to the transactions. For example, the \$6,000 expenditure by the Santa Barbara foundation which was considered questionable is explained as follows:

On Vernon Cheadle's retirement as Chancellor of UCSB, approximately sixty of his friends gave one hundred dollars each to purchase him a membership in the Birnam Wood Golf Club, Santa Barbara as a retirement gift. Benefit to the University would accrue as the membership would enable Dr. Cheadle to conduct University public relations work in a forum otherwise unavailable. Donors were solicited for one hundred dollar gifts restricted to the particular golf club membership and were advised in writing that the contribution should not be considered tax deductible.

(5/)

Also questioned, as listed in Appendix C, are "direct purchases for goods and services, bypassing U.C. purchasing channels." As legal entities, the foundations have no obligation to utilize U.C. services.

With respect to information omitted from federal tax returns the following information has been provided by the foundations:

Political contributions were not made by the UCLA Foundation. A director of the Foundation made unauthorized contributions and then improperly sought and received reimbursement from the Foundation. As the audit report notes, the Foundation has recovered this outlay through cash restitution and by a secured promissory note.

(6/)

The Cal Aggie Foundation, in the absence of additional detail, has not been able to verify that political contributions were made.

(7/)

The Santa Barbara Foundation is consulting with counsel and external auditors to determine if amended information returns should be filed as a result of purchases of securities (through foundation trustee) from a stock brokerage firm with which such trustee is affiliated.

On page 15 of the audit report it is indicated that at UCLA additional compensation payments have been made to foundation officers or employees whose salaries were being paid through the university payroll system. This is not an accurate statement. One University employee, the Assistant Chancellor-- Alumni & Development, is an officer of the Foundation, serving as secretary. His salary is paid by the University, and not the Foundation. All other officers are volunteers who serve without remuneration. The General Counsel of the Foundation serves in that position as a volunteer without remuneration, although his law firm is remunerated on a reduced-fee basis for legal services it may perform for the Foundation.

(8/)

It should be noted that the listing in Appendix C of the ten general categories of expenditures challenged as questionable includes some expenditures which reflect the consciously different policies of the private foundations, are entirely consistent with their fundraising activities and are common to many private charities.

While it is acknowledged that there is room for improvement in the foundations' procedures and controls, it is believed that the unqualified presentation of unaudited transactions in Appendix C creates a mistaken impression of the degree of improprieties which have occurred in foundation operations.

9/

EXHIBIT I

January 13, 1975

CHANCELLORS
PRINCIPAL OFFICERS OF THE REGENTS
ADMINISTRATIVE OFFICERS, OFFICE OF THE PRESIDENT

Ladies and Gentlemen:

Subject: Policy Governing Entertainment

The attached policy statement governing official University entertainment supersedes the current policy concerning this subject issued on January 21, 1970, and it is effective February 1, 1975.

You will note that the format of the policy statement has been changed so that future rate changes may be made without having to reissue the complete policy.

Sincerely,



G. O. McCorkle, Jr.

Attachment

cc: President Hitch
Assistant Vice President Everett
Vice Chancellors--Administration/
Business & Finance
Accounting Officers

POLICY GOVERNING ENTERTAINMENT

I. PURPOSE

There are occasions in which judicious extension of hospitality is in the best interest of the University. It is essential that the expenditure of University funds for entertainment be prudent and in a manner which is in keeping with accepted standards of the educational community and compatible with the University's status as a tax-supported institution.

This policy governs the manner and extent to which the University may extend hospitality in the form of meals and entertainment.

II. WHEN EXPENDITURES MAY BE MADE

Whenever the University acts as host, the occasion must, in the best judgment of the approving authority, be of significance in the affairs of the University and not of the type that the responsible individual would normally undertake in a personal rather than an official capacity. As a guide in reaching this decision, the approving authority must evaluate the importance of the event in terms of the costs that will be incurred, the benefits that are anticipated from this expenditure, the availability of funds, the alternatives that would be equally effective in accomplishing the desired objective. Occasions for which the expenses of official entertainment satisfactorily meeting this multiple standard may be approved include but are not limited to the following:

- A. When the University is host or sponsor of a meeting of a learned society or organization, the costs of meals or light refreshments may be defrayed by the University.
- B. When the University is host to official guests or to prospective appointees for positions requiring specialized training, and/or experience of a professional, technical, or administrative nature, the costs of meals or light refreshments may be defrayed by the University.

An official guest shall be defined as a person not otherwise employed or compensated by the University who renders a service to the University and/or is present at the University at the invitation of or as a guest of the person authorized to approve the expenditure.

- C. When meetings of an administrative nature are held which are directly concerned with the welfare of the University, the costs of meals or light refreshments may be defrayed by the University. Where meals are involved, they must be a necessary and integral part of the business meetings, not a matter of personal convenience.

- D. When meetings between faculty or administrators and students are held, the costs of light refreshments may be defrayed by the University.

III. AMOUNTS AUTHORIZED

Attachment A to this policy sets forth the maximum allowed for entertainment. A University employee who serves as official host or participates at the request of the official host and who is in travel status and eligible for per diem shall deduct the equivalent allowance for the meal(s) from the per diem claimed for that day (Business and Finance Bulletin G-28, Policy and Regulations Governing Travel, Section XI.D.).

IV. APPROVAL OF EXPENDITURES

Approval of expenditures for official entertainment must be obtained at the appropriate level, prior to incurring the expense. Approval of such expenditures shall be authorized by the President, Vice Presidents, Chancellors, Principal Officers of The Regents, or their designated representatives. Delegations of this authority must be in writing, with copies to the appropriate Accounting Officer.

V. SOURCE OF FUNDS

Expenses for official entertainment may be defrayed from various University fund sources, within the existing level of Supplies and Expense funds, and are subject to the above rules and the following general limitations:

<u>Source</u>	<u>Limitation</u>
State Appropriations	No alcoholic beverages or tobacco purchases.
Various non-State funds of the University	Observe restrictions, if any, on use of the fund.
Extra-mural (contracts and grants) funds	If specifically authorized in the contract or grant or by agency policy and to the extent and for the purpose(s) authorized. (Terms of an award cannot authorize an expenditure which is not in accordance with University policy, as outlined herein.)

IV. PROCEDURES FOR CHARGING EXPENDITURES

Official entertainment charges may be processed as a direct charge to an appropriate account by any of the following means:

- A. Official entertainment may be claimed for reimbursement on a Form 5, "Request for the Issuance of a Check," supported by appropriate sub-vouchers.

- B. The President, Vice Presidents, Chancellors, Principal Officers of The Regents, or their designated representatives may establish a single commercial credit card account for direct charge of off-campus official entertainment expenses to one account; multiple credit cards may be issued. On-campus official entertainment may be charged to an appropriate account by these same officials or by persons to whom they have delegated approval authority pursuant to Section IV. above.

(Note instruction set forth in Section III. above pertaining to deductions for equivalent allowance for meal(s), required for certain stated situations.)

VII. SUPPLEMENTAL RULES

The President, Vice Presidents, Chancellors, Principal Officers of The Regents, or their designated representatives may adopt supplemental rules to meet special needs insofar as such supplemental rules do not conflict with this policy.

AUDITOR GENERAL'S FOOTNOTES TO U.C. RESPONSE

Footnote

Discussion

1/

The question of U.C. control over the University's foundations appears to be the issue presented by the U.C. in this section. On pages 4, 5 and 8 of our report we discuss in detail the unavoidable and close relationship between the U.C. and its foundations.

Our conclusion that the independence is not clearly established is based upon the fact that the foundations:

- Primary purpose is to solicit gifts to further programs of the University,
- Have university officers or staff acting as foundation trustees, directors or officers,
- Utilize university assets rent-free,
- Maintain offices on the university campuses, and
- Utilize university accounting systems.

Furthermore, the fact that three campuses (page 9 of our report) have established controls over their foundations, proves that the University can control the foundations, and have.

Footnote

Discussion

2/

The wording of the cited sentence was changed on the final draft to read: "The propriety of the expenditures was measured against existing university guidelines governing expenditure payments or reimbursements to determine whether the expenditures incurred by the foundations would have been allowable under university rules and regulations." (See page 5.)

3/

On page 7 of the report we summarized our understanding of the July 1976 letter from the U.C. President. The quote given by U.C. in response is incomplete, and as a result, leads the reader to believe that there was no basis for our conclusion. The verbatim quotation from the President's July 1976 letter is:

3. Gifts to The Regents shall be administered in accordance with established University policies and practices and, to the extent practicable, gifts for the benefit of the University to campus foundations shall also be administered in accordance with University policies.

4/

The response suggests that it is not appropriate for the University to issue guidelines governing the allowability of foundation expenditures, while on pages 9, 10 and 11 of our report we describe policies established by four U.C. campuses which directly affect foundation expenditures.

Footnote

Discussion

5/

The facts surrounding the \$6,000 golf club membership at U.C. Santa Barbara are correctly stated in the response. It was presented to depict an expenditure made through the foundation which would not be allowed through U.C. channels. The contributors of the other \$16,985 we identified, however, were not advised that contributions should not be considered tax deductible nor were they advised as to the nature of the expenditure.

6/

Although the political contributions were reimbursements to the former UCLA Foundation Director the documentation supporting the reimbursement by the foundation clearly established that the purpose of the expenditure was political in nature.

7/

We were in contact with the Cal Aggie Alumni Foundation during the response period and detailed the expenditures we identified. We will again contact them to assure proper notification.

8/

The persons identified in the response were not the basis for our conclusion. Our conclusion is based on the UCLA Foundation's Director of Business and Finance who received \$1,500 in additional compensation in September 1975.

Footnote

9/

Discussion

Appendix C in the discussion draft issued to the U.C. contained the caption "unaudited" pending our final review of the working papers. The inference that our work supporting Appendix C is "unaudited" is not correct. We have vouched and verified each transaction listed in the Appendix following the audit scope described in our report on page 5.

SURVEY OF U.C. FOUNDATIONS: COMPARISON OF THE
LEGAL STATUS AND AUTONOMY OF CAMPUS FOUNDATIONS
(DATES OF SURVEY--9/12/77 THROUGH 11/14/77)
University of California Campuses

Questionnaire	California Aggie Alumni Foundation, Davis	University of California, Berkeley Foundation	The UCLA Foundation, Los Angeles	The UCI Foundation, Irvine	UC San Diego Foundation, San Diego	UC Riverside Foundation, Riverside	The UCSB Foundation, Santa Barbara	UC Santa Cruz Foundation, Santa Cruz	UCSF Foundation, San Francisco
1. Is your Foundation completely autonomous and/or legally separated from U.C.?	yes	yes	yes	yes	yes	yes	yes	yes	yes
2. Is your Foundation's accounting system completely independent of the U.C.'s accounting office?	yes	yes	yes	yes	yes	yes	yes	no	yes (Note 3)
3. Does your Foundation hire consultants to assist in its fund-raising activities?	no	yes	yes	no	no	yes	no	no	no
4. Do Foundation officers also hold positions within the administration of the University? If yes, do Foundation officers serve with remuneration?	yes no	yes yes	yes yes	yes yes	yes no	yes no	yes no	yes no	yes no
5. What is the relationship between the Foundation and the U.C.'s Alumni Association?	Notes 1&2	Notes 1&2	Notes 1&2	Notes 1&2	Notes 1&2	Note 1	Note 1	Notes 1&2	

NOTES: (1) Fund-raising activities of the Foundation are integrated with those of the Alumni Association and the U.C. campus.

(2) Certain fixed assets belonging to the U.C. Regents are used rent-free by the Foundation.

(3) The Foundation has been incorporated but is not operative at this time.

SURVEY OF SELECTED STATE UNIVERSITIES: COMPARISON AS TO
LEGAL STATUS AND AUTONOMY OF CAMPUIS FOUNDATIONS
(DATES OF SURVEY - 9/12/77 THROUGH 1/14/77)
Other State Universities

Questionnaire	University of Illinois Foundation	University of Iowa Foundation	University of Washington	University of Minnesota Foundation	University of Michigan	State of New York Foundation	Ohio State University	Penn State Foundation	University of Texas Foundation	Indiana University Foundation
1. Is your Foundation completely autonomous and/or legally separated from your State University?	yes	yes	Note 1	yes	Note 1	yes	Note 2	no	yes	Note 3
2. Is your Foundation's accounting system completely independent of the State University's accounting office?	no	yes		yes		yes		no	yes	
3. Does your Foundation hire consultants to assist in its fund-raising activities?	yes	yes		yes		yes		yes	no	
4. Do Foundation officers also hold positions within the administration of the University? If yes, do Foundation officers serve with remuneration?	yes	no		yes		no		no	yes	
5. What is the relationship between the Foundation and your State University's Alumni Association?	Separate legal entities.	Separately incorporated organizations, but work closely together.		Independent entities, but work closely together.		Both entities play a role in the development and fund-raising programs.		Both directors report to the same senior officer of the University.	none	

NOTES: (1) The University has no foundation.

(2) The University does not operate a "foundation." The Ohio State University Development Fund is created as the official agency for the solicitation of funds for the University.

(3) No response was received from the University up to the close of our survey.

UNIVERSITY OF CALIFORNIA
SAMPLES OF EXPENDITURES INCURRED BY SELECTED U.C. CAMPUS FOUNDATIONS
FOR THE FISCAL YEARS 1975-76 AND 1976-77

Item No.	Expenditure Category	Fiscal Year	Total		The UCLA Foundation		Cal Aggie Alumni Foundation		The UCSB Foundation		U.C. Santa Cruz Foundation	
			Number of Cases	Amount	Number of Cases	Amount	Number of Cases	Amount	Number of Cases	Amount	Number of Cases	Amount
Expenditures Which Would Not Have Been Allowed by the U.C.												
1	First-class air fares (difference between first-class and coach)	1975-76 1976-77	10 --	\$ 3,296 --	5 --	\$ 509 --	5 --	\$ 2,787 --				
2	Purchases of liquor and other alcoholic beverages	1975-76 1976-77	19 7	5,327 2,596	9 3	3,931 2,207	10 1	1,396 189			3	\$200
3	Direct purchases for goods and services, bypassing U.C. purchasing channels	1975-76 1976-77	4 3	10,089 3,825	1 3	4,791 3,825	3 --	5,238 --				
4	Memberships in organizations which are primarily social	1975-76 1976-77	8 5	15,502 7,483	8 4	15,502 1,483	-- --	-- --	1	\$6,000		
5	Unusual entertainment bills including meals in excess of maximum allowable	1975-76 1976-77	11 8 75	28,163 12,915 \$89,196	10 8 51	24,015 12,915 \$69,178	1 -- 20	4,148 -- \$13,818			3	\$200
Expenditures Which Were Incurred Contrary to the Provisions of the Articles and By-Laws Including Questionable and Not Properly Documented Expenditures Prior to Payment												
6	Travel advances for which no accounting was rendered upon completion of trip	1975-76 1976-77	10 2	\$ 9,836 2,796	3 2	\$ 4,288 2,796	7 --	\$ 5,548 --				
7	Other payments unusual or personal in nature	1975-76 1976-77	45 20	15,282 8,379	11 9	10,819 2,397	34 11	4,463 5,982				
8	Double payment of air travel expenses	1975-76 1976-77	-- 3	-- 1,652	-- --	-- --	-- 3	-- 1,652				
9	Payments unsupported or with inadequate documentation	1975-76 1976-77	10 8	5,969 31,986	-- 5	-- 18,040	10 3	5,969 13,946				
10	Political contributions	1975-76 1976-77	3 4 105	7,035 4,940 \$87,875	2 3 35	7,000 4,800 \$50,140	1 1 70	35 140 \$37,735				

Office of the Auditor General

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
Secretary of State
State Controller
State Treasurer
Legislative Analyst
Director of Finance
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
California State Department Heads
Capitol Press Corps